The Marcos Presidency and Martial Law

Marcos immediately sought to accelerate growth through expansionary fiscal and monetary policies. The government greatly raised capital expenditures, especially on infrastructure—irrigation, roads, schools, and communications—in rural areas. Between 1964 and 1968, government expenditures rose by 43 percent in real terms from 11.5 percent to 14 percent as a percentage of GNP. Domestic credit was relaxed by the central bank; according to one study, credit increased by 40 percent between 1965 and 1967—more than twice the rise of nominal GNP.[62] GNP also grew, but the price of that growth was balance-of-payments and debt-service problems. As a percentage of GNP, external debt grew from 13 percent in the 1965-1968 period to 33 percent in 1970. Marcos himself stated that servicing the Philippines' debt in 1970 would "take over half our export earnings."[63] The International Monetary Fund and other credit institutions persuaded the Philippine government to implement a stabilization program that included cutting government expenditures and devaluing the peso. By the end of 1970, the peso's value had dropped by 43 percent relative to the dollar.

The early 1970s was a period of stabilization. External debt fell as a percentage of GNP, which was growing at a brisk pace (see Table 5). The current account went from deficit to surplus. But real wages declined between 1969 and 1973, despite a rising per capita GNP. The lower wages and the low value of the peso fueled the Philippines' exports, but that did not "translate into improvements in the lot of Filipino masses."[64]

Shortly after declaring martial law in 1972, Marcos sharply expanded the role of government in development. He formed the National Economic and Development Authority (NEDA) to plan it. The state took ownership of the Philippine Airlines, multinational oil companies sold their stakes to the state-owned Philippine National Oil Company, and the military acquired several private steel mills to form the National Steel Corporation.[65] Technocrats armed with economics, business, and engineering degrees increasingly staffed the bureaucracy.

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62. Dohner and Intal, "The Marcos Legacy," p. 383.

63. Quoted in Dohner and Intal, "The Marcos Legacy," p. 382.

64. Ibid., pp. 383-384.

65. Bela Balassa, *Economic Policies in the Pacific Area Developing Countries* (New York: New York University Press, 1991), p. 166.

TABLE 5. ECONOMIC INDICATORS FOR THE PHILIPPINES, 1965-1973
(As a percentage of gross national product)

Indicator	1965-1968	1969	1970	1971	1972	1973
Real GNP (Percentage growth)	4.9[a]	5.2	3.9	6.5	5.4	9.3
Budget Surplus	-0.7	-3.5	0.2	-0.5	-2.4	-1.2
External Debt	13	22	33	27	26	22

SOURCE: Congressional Budget Office based on data from Robert S. Dohner and Ponciano Intal, Jr., "The Marcos Legacy: Economic Policy and Foreign Debt in the Philippines," in Jeffrey D. Sachs and Susan M. Collins, *Developing Country Debt and Economic Performance*, vol. 3, *Country Studies—Indonesia, Korea, Philippines, Turkey* (Chicago: University of Chicago Press, 1989), p. 384.

NOTE: GNP = gross national product.

a. Annual average.

Government expenditures rose after martial law was established in 1972 (see Table 6). By increasing the level of foreign borrowing, Marcos dramatically raised public investment. By 1978, it had risen to 7 percent of GNP, or 30 percent of total domestic capital formation.

For a few years Marcos's program seemed to work. GNP per capita grew at a vigorous average annual rate of 3.0 percent between 1973 and 1979. In addition, international prices for many of the Philippines' primary exports, such as copper and wood, rose dramatically. That growth, and massive increases in government spending, enabled the economy to weather the first oil crisis in 1973-1974.

The Philippine export base diversified during the 1970s. In 1970, over 90 percent of exports were primary or slightly processed commodities. By 1979, that proportion had fallen to 50 percent. In their place were labor-intensive, nontraditional manufactured exports. The manufacture of some goods for export contained a large amount of imported materials and thus required substantial foreign exchange to pay for them. But the government managed that debt carefully, and debt service did not increase very much as a percentage of export earnings. As a percentage of GNP, the Philippines' external debt was comparable with Korea's.

The average Filipino, however, did not participate in those economic gains. Real wage rates for agricultural workers declined by 25 percent between 1966 and 1986 (see Table 7). Urban workers, both skilled and unskilled, fared even worse: their real wages declined by 69 percent and 73 percent during the same period. Thus, although the economic pie was growing larger, the distribution of that pie appeared to be shifting against the poorest segments of the population. Between 1971 and 1985, the percentage of the population living in poverty increased dramatically, as shown below:[66]

Year	Percentage of Population in Poverty
1965	41.0
1971	43.8
1975	51.5
1985	58.9

66. Boyce, *The Philippines: The Political Economy of Growth and Impoverishment*, p. 46. Data on poverty should be treated with caution. Researchers have been unable to explain how poverty could increase and wages decline while per capita GNP increased during the 1970s. Moreover, poverty is not a clearly defined concept. In the Philippines, poverty lines have been based on estimates of the income needed to meet nutritional requirements. However, if the income of poor families has been understated over time, it could dramatically affect estimates of poverty trends. Furthermore, defining poverty in that manner gives no indication of how far below the poverty line people are.

TABLE 6. ECONOMIC INDICATORS FOR THE PHILIPPINES, 1973-1979
(As a percentage of gross national product)

Indicator	1973	1974	1975	1976	1977	1978	1979
Real GNP (Percentage growth)	9.3	5.6	5.8	7.4	6.3	5.8	6.9
Government Expenditure	14.3	11.7	16.0	15.2	14.9	14.8	13.7
Budget Surplus	-1.2	0.5	-1.6	-1.8	-1.9	-1.2	-0.2
Investment	21.9	26.7	30.6	31.3	29.0	29.1	31.0
Saving	27.0	25.4	25.3	25.4	25.8	24.4	26.6

SOURCE: Congressional Budget Office based on data from Robert S. Dohner and Ponciano Intal, Jr., "The Marcos Legacy: Economic Policy and Foreign Debt in the Philippines," in Jeffrey D. Sachs and Susan M. Collins, *Developing Country Debt and Economic Performance*, vol. 3, *Country Studies—Indonesia, Korea, Philippines, Turkey* (Chicago: University of Chicago Press, 1989), pp. 389, 391.

NOTE: GNP = gross national product.

TABLE 7. STANDARD-OF-LIVING INDICATORS FOR THE PHILIPPINES, 1962-1986

Indicator	1962	1966	1970	1974	1978	1982	1986
Wage Rate[a]							
Agricultural worker	100	93.6	75.9	54.2	87.6	65.0	70.7
Skilled urban worker	100	89.1	89.5	55.3	54.0	48.8[b]	27.8
Unskilled urban worker	100	96.1	103.3	63.0	57.2	41.1[b]	25.7
Unemployment Rate	21.8[c]	22.0	14.9[d]	10.6	14.7	24.1	22.9
Prices[e]							
Food	20.4	27.6	33.4	74.5	100	162.5	329.1
Nonfood	27.8	29.6	36.1	70.1	100	186.3	387.3

SOURCE: Congressional Budget Office based on data from James K. Boyce, *The Philippines: The Political Economy of Growth and Impoverishment in the Marcos Era* (Honolulu: University of Hawaii Press, 1993).

a. Real daily wage rate index: 1962 = 100.

b. Value shown is for 1983; value for 1982 is not available.

c. Value shown is for 1961; value for 1962 is not available.

d. Value shown is for 1971; value for 1970 is not available.

e. Real food price index: 1978 = 100.

The Economic Crisis of the 1980s

The economic situation in the Philippines deteriorated rapidly after the second oil shock in 1979-1980. Between 1980 and 1986, total GNP declined and per capita GNP fell by an average of 3.3 percent a year. Export earnings also dropped 5 percent a year from 1980 to 1983. The government tried to alleviate those conditions by increasing its expenditures and foreign borrowing. The external debt grew from 52 percent of GNP in 1980 to 93 percent in 1985. But foreign and domestic investors lacked the confidence that the economic problems were short term. Net foreign investment declined to almost nothing, and capital flight may have reached 5 percent of GNP in 1981 and 1982.[67]

In an effort to stem the decline, the government made a severe adjustment. Investment as a share of GNP declined by more than 50 percent between 1980 and 1985 (see Table 8). Government expenditures were cut to control inflation, which exceeded 50 percent in 1984. By the time Marcos left office in 1986, external debt was nearly equal to GNP. Income levels were no higher than they had been in 1974.

Four factors contributed to this state of affairs. First, the high level of public-sector investment did not translate into higher rates of economic growth. Second, the Philippines financed that investment through foreign borrowing. The government continued to borrow, it was unable to raise resources domestically, and export earnings were not growing fast enough to service the debt. The government maintained overvalued exchange rates and protectionist trade policies, which had a particularly negative impact on the agriculture sector, the source of much of the Philippines' foreign exchange. Imports of food products were cheap relative to domestic production, which tended to reduce farmers' income and production. Third, the absence of land reform contributed to the high incidence of poverty in rural areas.

Last and perhaps most important was corruption in the Marcos government. The government borrowed abroad to invest domestically. At every step in that process, there were bribes and kickbacks and other forms of self-aggrandizement by Marcos, his family, and his friends. According to Erik Thorbecke, the very purpose of the borrowing and the investment in many cases was to divert resources in the planning and construction phases.[68] The government was often obligated to pay back the loan even though it generated little return to the country. As one scholar put it, "to a real extent, the Philippines under martial law developed a [self-serving]. . .

67. Dohner and Intal, "The Marcos Legacy," p. 393.

68. Thorbecke, "The Political Economy of Development," p. 29.

TABLE 8. ECONOMIC INDICATORS FOR THE PHILIPPINES, 1980-1988

Indicator	1980	1981	1982	1983	1984	1985	1986	1987	1988
Real GNP (Percentage growth)	5.0	3.4	1.9	1.1	-7.1	-4.1	2.0	5.9	6.7
External Debt (Percentage of GNP)	49.0	n.a.	62.8	72.7	80.6	81.7	92.9	84.1	n.a.
Investment (Percentage of GNP)	30.7	30.7	28.8	27.5	19.2	14.3	13.2	15.4	18.2
Debt Service[a]	20.8	n.a.	38.1	38.2	43.4	36.9	34.0	35.3	n.a.

SOURCE: Congressional Budget Office based on data from Robert S. Dohner and Ponciano Intal, Jr., "The Marcos Legacy: Economic Policy and Foreign Debt in the Philippines," in Jeffrey D. Sachs and Susan M. Collins, *Developing Country Debt and Economic Performance*, vol. 3, *Country Studies—Indonesia, Korea, Philippines, Turkey* (Chicago: University of Chicago Press, 1989): pp. 392, 394.

NOTE: GNP = gross national product; n.a. = not available.

a. Total interest payments plus amortization of total medium- and long-term debt as a percentage of exports of goods and services.

government which over time would sap the energy of the domestic economy and which contributed significantly to the economic crisis of the 1980s."[69]

Economic Policy Under Aquino and Ramos

Economic policy under Corazon Aquino, who assumed the presidency in 1986, did not immediately resolve the Philippines' problems, but it made progress. Economic growth improved in the first few years after the fall of Marcos, largely as a result of a stabilization and adjustment program that the International Monetary Fund had imposed during the last few years of the Marcos government. GNP grew 4 percent a year between 1986 and 1992. Between 1987 and 1992, GNP per capita grew at an average annual rate of 1.9 percent. Some major changes included establishing a neutral export regime, reforming the tax and financial system, and curbing government intervention in the economy. However, not all problems were solved. For example, the depletion of natural resources continued, especially in the watersheds and fisheries, and poverty remained high.

In 1992, Fidel Ramos was elected to the presidency. He intended to carry out a comprehensive economic reform program. Ramos largely succeeded in reducing tariff barriers, privatizing state-owned industries, reducing external debt, cutting government expenditures, increasing private investment in infrastructure, increasing GNP, and reducing the poverty rate.

The Philippines seems on track to greater sustained growth. Many analysts believe that it has broken the cycle from its past. Yet there is some concern that this progress is dependent on Ramos, whose term expires in 1998 and who cannot run for reelection. And "crony capitalism," in the words of AID, "is not yet dead."[70]

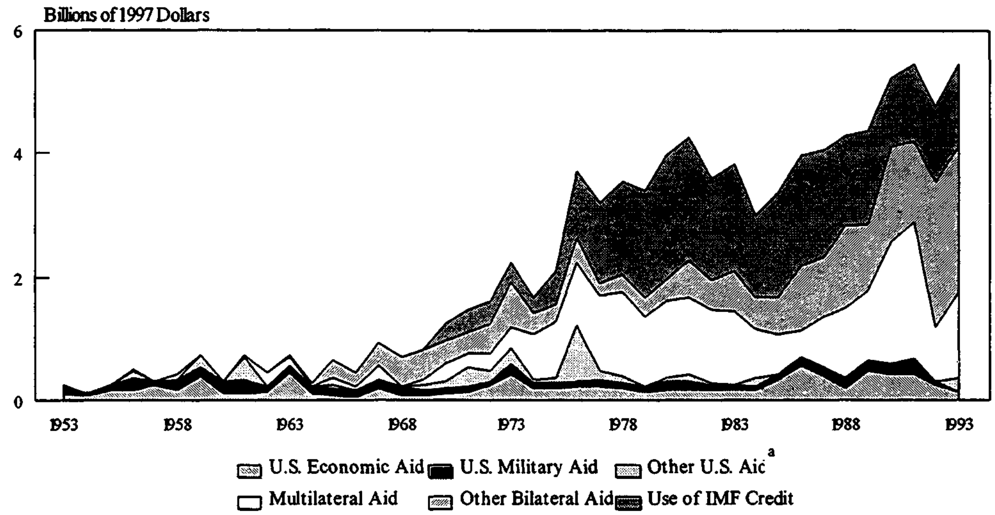
ROLE OF FOREIGN ASSISTANCE IN THE PHILIPPINES' DEVELOPMENT

The Philippines has received foreign assistance from a variety of sources during the past 40 years (see Figure 3). U.S. economic and military assistance accounted for two-thirds of the aid to the Philippines in the 1950s and 1960s. The World Bank

69. Dohner and Intal, "The Marcos Legacy," p. 389.

70. Agency for International Development, *Congressional Presentation: Fiscal Year 1996* (February 24, 1995), p. 332.

FIGURE 3. FOREIGN ASSISTANCE TO THE PHILIPPINES, 1953-1993



SOURCE: Congressional Budget Office based on data from the Agency for International Development, the World Bank, and the Organization for Economic Cooperation and Development..

NOTE: IMF = International Monetary Fund.

a. Mostly loans from the Export-Import Bank.

began lending to the Philippines in 1958 and eventually became a primary provider of foreign assistance to the Marcos government. The Asian Development Bank began lending to the Philippines in 1969. Other countries, particularly Japan, have also given assistance.

U.S. assistance was motivated partly by strategic considerations. The United States did not want to see the Philippines succumb to a communist-backed insurgency. Since a communist government was avoided, U.S. aid in one sense succeeded. But the aid may also have undermined the development goals of U.S. assistance.

Health

The role of foreign aid in the health sector is difficult to evaluate, but health indicators did improve. Between 1961 and 1993, the United States, the World Bank, and the Asian Development Bank allocated about 7 percent of their economic assistance to health. Infant mortality rates fell from 72 deaths per thousand in 1967 to 44 in 1992. The United States appeared to put particular emphasis on reducing infant mortality through various child survival programs.[71] Other measures also indicate improvement. For example, crude death rates—deaths per thousand—have declined, and life expectancy has increased.

Education

The population of the Philippines, like that of South Korea, has been well educated for some time. The literacy rate in 1970 already exceeded 80 percent. In 1992, the rate was 90 percent. Between 1961 and 1993, AID, the World Bank, and the Asian Development Bank allocated about 4 percent of their economic assistance to education. An AID evaluation describes the building of schools as one of its most "consistently successful" programs. Between 1980 and 1991, U.S. money helped build more than 2,300 school buildings—improving the standard of living and educational levels in the communities they serve. A school building is often the most well constructed building in a rural community and serves as protection for an entire town during severe storms, such as typhoons.[72]

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71. Benjamin P. Loevinsohn, *Setting Quantitative Objectives in Health Sector Programs: Lessons Learned from the Philippine Child Survival Program*, CSP Monograph No. 3 (Manila: Department of Health, Republic of the Philippines, 1993).

72. Agency for International Development, "AID Evaluation in Summary, Part 1," in *AID Impact Evaluation: Economic Support Fund Infrastructure Program, 1980 to 1991* (May 1991), p. 1.

Population Growth

In 1967, the Agency for International Development began providing assistance to the Philippines to deal with issues related to population. AID trained and supported personnel who staffed various clinics and other organizations. It also supported various methods of contraception. During the Marcos era, AID's population activities were highly integrated with those of the Philippine government. Those efforts, however, encountered some hostility from the Aquino government. Overall, major donors have not allocated a large percentage of their aid to population issues. Between 1961 and 1993, the United States, the World Bank, and the Asian Development Bank allocated approximately 1 percent of their economic assistance to population programs.

The Philippines has seen a slowing of population growth and a falling fertility rate. The prevalence of various methods of contraception, particularly voluntary sterilization and the pill, have grown substantially—from 15 percent to 36 percent between 1968 and 1988. Problems in those programs have included inadequate training, weak field supervision of programs, and some poorly conceived incentive programs. Although the fertility rate has declined, AID does not claim credit. In an evaluation of its contraceptive program, the agency stated that "fertility has continued to decrease at a rate that cannot be accounted for by the methods in which A.I.D. has made its greatest investment."[73]

Agriculture

Judging the usefulness of the agricultural aid provided by AID, the World Bank, and the Asian Development Bank is also difficult. Those organizations spent over 20 percent of their assistance on agriculture. Sectoral evaluations of efforts by the World Bank and the Asian Development Bank are not available, but a 1987 AID evaluation of its projects reported that its Bicol River Basin Development Program provided substantial benefits to one of the poorest regions of the Philippines. AID spent $29 million on that project—a small fraction of U.S. money spent in the agriculture sector. Household income in the area grew, irrigation increased, and crop yields rose substantially.[74]

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73. Agency for International Development, Center for Development Information and Evaluation, *Evaluation of AID's Family Planning Program in the Philippines*, AID Evaluation Highlights No. 11 (1992), p. 8.

74. Agency for International Development, Asia Near East Bureau, *The Impact of U.S. Development Assistance in Asia and the Near East* (1987), pp. 127-128.

The United States contributed relatively small amounts to agricultural research. But when combined with resources from other donors and the government of the Philippines, that aid yielded some impressive results. Those results included a first-class agricultural university and research efforts that eliminated diseases and increased agricultural yields, particularly for small farmers. The financial return of those efforts, according to AID, far exceeded their costs.

The broader picture, however, appears less positive. Although rice yields and those of agricultural products grown for export have risen since the 1960s, the benefits have accrued largely to the wealthy segments of Philippine society and, during the Marcos years, to Marcos and his allies in particular. Agricultural wage rates declined under Marcos, and the rural poor suffered considerably. In the absence of reform and improvements in many other areas—such as the overall policy environment—most Filipinos who worked in agriculture were not better off.[75]

Economic Growth

Not much is known about the effectiveness of U.S. aid programs to the Philippines during the 1950s and 1960s. U.S. money spent on building infrastructure produced some positive results, but at that time AID did not require systematic evaluations of the impact of its projects. Hence, CBO is unable to determine whether those projects were maintained, for example, or whether they had a negative environmental impact.[76]

Foreign aid provided to the Philippines under Marcos may have actually hurt the country's development by reinforcing his economic mismanagement and corruption. Between 1966 and 1986, the international community gave or lent approximately $33 billion (in 1997 dollars) to the Philippines, most of which was intended to promote economic growth. But per capita GNP averaged only 0.8 percent growth per year during that period. Moreover, poverty increased, and rural and urban wages declined dramatically. The Philippines' external debt as a percentage of GNP grew from 13 percent in the mid-1960s to 93 percent in 1986. And calculations of capital leaving the Philippines between 1962 and 1986 totaled over $19 billion, not including an adjustment for lost interest. Before being driven

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75. Boyce, *The Philippines: The Political Economy of Growth and Impoverishment*, p. 155.

76. Chris Hermann, *U.S. Assistance for Infrastructure Development from 1946 to 1995: Fifty Years of Accomplishment* (Agency for International Development, May 26, 1995), p. 10.

from power, Marcos, his family, and close associates "recycled" a substantial amount of the Philippines' external borrowing by sending or taking it out of the country.[77]

A long-term AID study on the building of infrastructure during the Marcos years reported positive results, especially in rural areas. Although very little information exists about the economic and social impact of infrastructure projects between the early 1960s and 1973, AID asserts that "it is fair to conclude that the construction of roads, bridges, irrigation systems and other small-scale projects helped meet local infrastructure [needs]."[78] During the period of martial law, AID continued to support many infrastructure projects designed to expand development in rural areas. Here, again, it is difficult to evaluate their impact on development. On the one hand, some analysts claim that many of those projects must have provided benefits to the populations and regions that they served, because the amount of resources going into infrastructure development was far greater than in any other sector. On the other hand, the actual record of per capita GNP growth under Marcos is uninspiring. If foreign aid projects were improving the conditions of the poor, the improvement did not show up in aggregate national indicators.

After Marcos was driven from power in 1986, the major foreign aid donors joined together in a cooperative assistance program to the Aquino government—the Multilateral Assistance Initiative (MAI). The MAI was an effort led by the United States to rally the international community to help rebuild the Philippine economy and support democracy. The reform program of Corazon Aquino and Fidel Ramos, Aquino's successor, has received strong support from the MAI donors. The United States, the International Monetary Fund, and the World Bank played critical roles in helping amplify, fine-tune, and promote the reform agenda.

The MAI also funded various regional development activities, placing particular emphasis on building infrastructure. Although determining the precise responsibility of foreign aid is difficult, those efforts helped build an economy that has flourished since the early 1990s. In 1995, Philippine Finance Secretary Roberto de Ocampo credited the MAI with helping bring that about: "A large part of the credit for our dramatic turnaround and persistent push towards a track of high growth can be owed to strong international support—specifically to the Multilateral Assistance Initiative."[79]

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77. Boyce, *The Philippines: The Political Economy of Growth and Impoverishment,* pp. 279, 295, 297. Some estimates put the amount in the billions of dollars.

78. Hermann, *U.S. Assistance for Infrastructure Development from 1946 to 1995*, p. 26.

79. Quoted in Agency for International Development, *The Philippines: Results Review and Resource Request* (March 1996), p. 5.

In comparing the development histories of South Korea and the Philippines, several observations seem particularly important. First, military expenditures did not seem to hinder development. Throughout the past 40 years, South Korea has devoted a greater percentage of its GNP to the military than the Philippines.

Second, the economic policy environment was probably the most important determinant of development. South Korea's inward-looking economic policies in the 1950s hindered its development, whereas the outward-looking policies of succeeding decades spurred economic growth. Marcos pursued economic policies that were similar to Rhee's in Korea during the 1950s, resulting in extremely slow growth, a large external debt, and a fragile, underdeveloped economy.

Third, Korea's moderate levels of corruption under the Park regime did not substantially undermine its growth prospects so long as it maintained an outward-looking, export-oriented economic policy. The high levels of corruption under Marcos, however, played an important role in undermining the Philippines' development, exacerbating the damage done by inward-looking economic policies.

Fourth, foreign aid is less effective when it is given for political as well as developmental reasons. Rhee knew that the United States was committed to supporting him and therefore was unwilling to make reforms. When that commitment seemed to waver in the late 1950s, he began to make some changes. Similarly, in the 1970s and 1980s, Marcos received aid from the United States in part because the United States did not wish to see his government fall to a communist insurrection.

Fifth, foreign bilateral and multilateral assistance appears to have improved education and health regardless of the overall policy environment. Still, the right policy environment is likely to make investments in human capital more effective. With respect to economic growth, the case of Korea suggests that foreign aid can play a modest and positive role in promoting development in a favorable economic environment. The opposite argument is less clear. On the one hand, foreign assistance given to countries with unfavorable economic policies—Rhee's Korea, Marcos's Philippines—may contribute to development, for example, by building necessary infrastructure. On the other hand, to the extent that foreign aid sustained the Marcos government and helped keep it in power longer, foreign aid may have actually harmed the development of the Philippines because of the destructive effect of that government's policies.

These cases also suggest that a strong base of human capital is not enough. Education alone, for example, was insufficient to generate growth in the Philippines.

Both South Korea and the Philippines have had well-educated populations for decades, but Korea's economy has grown at a dramatic rate and the Philippines' has not.

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